This record is a partial extract of the original cable. The full text of the original cable is not available.

UNCLAS SECTION 01 OF 02 ABUJA 002087

SIPDIS

SENSITIVE

E.O. 12598: N/A
TAGS: ECON EFIN EPET PGOV NI OIL
SUBJECT: OIL PRICE IMPACT ON NIGERIA

REF: STATE 186514

¶1. (SBU) Summary: High oil prices have proved a very mixed blessing for Nigeria. While greatly boosting government revenues, they have increased the challenge of managing those revenues. Though the government is wisely directing much revenue to debt repayment, some of the windfall is finding its way to potential "white elephant" projects and exacerbating intra-government power struggles. Higher oil prices have complicated government efforts to deregulate the downstream petroleum sector. Nigeria's population has suffered through series of price hikes, without yet seeing the end of subsidized fuel. High fuel prices are having knock-on effects for other goods. The rising cost of fertilizer, in particular, will reduce Nigeria's low use and affect agricultural output. Shifts in demand and pricing are also causing the investment climate in the oil sector to evolve. Finally, high oil prices increase the incentive for oil theft and diversions. End Summary.

More Revenue, More Headaches

¶2. (SBU) With 85% of Nigeria's government revenue coming from oil, and with the GON getting a significant slice of oil earnings, including for the moment everything over $35 per barrel, revenue has tripled in the last several years. Given Nigeria's limited absorptive capacity, and limited ability to spend it revenue effectively, managing this windfall presents a challenge. Under the strong leadership at the Finance Ministry and with the support of the President, the GON has directed all revenue above a benchmark price of $27 per barrel into a special account, meant to help temper swings in oil prices. The Finance Ministry has determined to direct much this funding toward retiring Nigeria's debt to remove debt service obligations from future budgets. Still, some of the money is directed toward infrastructure investments that might not prove their worth. For example, some of the money is being used to build several gas-fired electric power plants, even though in the as yet unreformed power sector most plants are not covering their costs.

¶3. (SBU) Nor are the Finance Ministry's plans for stewardship of the windfall uncontroversial. The National Assembly passed a budget with a higher benchmark price for crude oil, allowing higher spending, but the President has refused to implement it. It is not clear the Assembly will approve the repayment of debt. In addition, the federal government legally controls only 48% of revenue, with the remaining 52% belonging to the states, many of whose governors do not support the proposed uses, which divert funds from their control. When the federal government ignores or overrides the National Assembly and the governors, even under the banner of good fiscal management, the rule of law is undermined.

Price of Reform Rises

¶4. (SBU) In order to attract investment into oil refining and other downstream processes, Nigeria has been seeking to remove subsidies and deregulate the downstream petroleum sector. Raising prices to market levels is one of the basic building blocks of that reform. Unfortunately, each increase in domestic prices has quickly been followed by a new increase in global oil prices, and despite a series of heavily protested price increases, the moving target of market prices has not yet been reached, constantly postponing the next stage of reform.

All Pain, No Gain

¶5. (SBU) For the average Nigerian these price increases are all there is to see from rising oil prices. Any material benefits have eluded those at the grass roots level. Rising fuel costs, which include not just petrol, but also kerosene commonly used for cooking, have contributed to rising prices for food and other basic goods. In rural areas, higher kerosene prices are forcing many to substitute wood, increasing tree cutting and environmental impact. Rising oil prices are also pushing up the cost of fertilizer. Nigeria already produces and imports too little to meet it needs,

and farmers use far less than the optimal amount. Higher prices are likely to reduce fertilizer intensity further, with a negative impact on agricultural output, and while further pushing up food prices.

Changing the Investment Climate

¶6. (SBU) Rising prices and shifting demand are affecting oil sector investment in Nigeria. It is bringing new investors, some with little experience. For longstanding partners, with the price per barrel $60 and upward, the government has agreed to talk to oil companies about rethinking how revenue above $35 per barrel is split. On the other hand, higher prices and profits are raising the pressure on oil companies to take responsibility for resolving a growing number of issues in Nigeria, such as refining, power generation and community development.

Temptation

¶7. (SBU) High prices and tight availability increase the already considerable incentives to steal oil and trade in domestic quotas. With oil at the heart of corruption in Nigeria, the growing returns make it harder to bring transparency to the system and to reduce the scope for skullduggery. CAMPBELL